THE EFFECT OF CORPORATE SOCIAL RESPONSIBILITY DISCLOSURE TO EARNINGS FORECAST ACCURACY

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ABSTRACT: This study is aimed to investigate earnings the effect of corporate social responsibility disclosure to earnings forecast accuracy. The study also considers financial opaqueness of companies as control variable. There are only few amount of study on the relationship between corporate social responsibility disclosures to earnings forecast. Samples in this study are companies listed in Indonesia Stock Exchange. The result shows that corporate social responsibility disclosure has affect forecast error negatively; this indicates that the more information disclosed in corporate social responsibility disclosure will lead to lower forecast error. The result in this study complements previous studies and provides some understanding on the importance of corporate social responsibility disclosure.

Keywords: Corporate Social Responsibility; Corporate Social Responsibility Disclosure, Earnings Forecast,

I. INTRODUCTION

Along with the globalization and increasing in social awareness, Corporate Social Responsibility (CSR) is getting people's attention. CSR is a concept about company's responsibility to its stakeholder which includes consumer, employees, shareholders, communities, and environment. The implementation of CSR in Indonesia reveals positive indications, makes it potential to be conducted continuously by entities. Some positive indication revealed such as the implementation of *Program Penilaian Peringkat Kinerja Perusahaan* (PROPER), CSR awards, State Owned Enterprise forum on community development, also establishment of division or department that handle CSR in many corporations.

There are so many definitions regarding Corporate Social Responsibility. The World Business Council for Sustainable Development (WBCSD) defines CSR as a continuing commitment by business to contribute to economic development while improving the quality of life of the workforce and their families as well as of the community and society at large. That definition has a similarity with what already mentioned on Act No. 40 of 2007 chapter 1. It defines CSR as a commitment of a company to take part in sustainability economic development in order to improve life and environment quality that eventually will give the benefit not only for the company itself but to anything around it.

Act No. 40 of 2007 article IV chapter 66 requires companies to issue annual report that include a report of corporate social responsibility activities. Companies are also required to implement the corporate social responsibility that is budgeted and accounted as an expense of the companies itself. The form and contents of annual report itself set by Indonesia Capital Market Supervisory Agency (BAPEPAMLK[1]) through *Keputusan Ketua Badan Pengawas Pasar Modal dan Lembaga Keuangan Nomor:* KEP-431/BL/2012 about The Submission of Annual Report by Listed Companies. Point 2.a discussed about general provision about what to be included in annual report, with one of the items is about the disclosure of corporate social responsibility. The details of the CSR disclosure then explained on point 2.h which should covers the policy, type of

[1] BAPEPAMLK is *Badan Pengawas Pasar Modal dan Lembaga Keuangan*

program and the cost of activity related to environment, employment practices, social and community development, and product responsibility.

Dhaliwal et al. (2012) examined the relationship between disclosure of nonfinancial information through stand-alone CSR reports as a proxy and analyst forecast accuracy using firm-level data from 31 countries. Indonesian companies mostly use sustainability report in annual report to disclose CSR activities. There are only few Indonesian companies issued a stand-alone CSR report. Therefore, this research will use the CSR disclosure in annual report as a proxy.

This research wants to know the value of disclosing CSR-related information to the company itself. The value refers to the financial indicator which is earning forecast made by independent parties. Then, does the disclosure of corporate social responsibility affect earnings forecast accuracy? The objective of this study is to examine and give empirical evidence of the relation of the relation of corporate social responsibility disclosure to earnings forecast accuracy in Indonesian listed companies from year 2009-2011.

II. THEORETICAL BACKGROUND AND HYPOTHESIS DEVELOPMENT

Financial Reporting

Financial report is a structural presentation of a financial position and performance of an entity. The purpose is to give information of a certain financial position and performance which will benefit most financial report users. Those financial report users are existing and potential investors, lenders, and other creditors. The users' decision making depends on the return they expect from an investment in those instruments.

There are so many users of financial report so it can't show the exact information needed by each user. The users of financial report are divided into two which are primary and non-primary users. The primary users are the investors, creditors, and lenders; the financial report is mostly made to give information to those users. While the non-primary users have to rely on the general purpose financial report for the financial information they need since the company report its financial information based on what primary users need.

Chapter 1 of SFAC 8 about Conceptual Framework for Financial Reporting mentioned that general purpose financial reports which are not designed to show the value of reporting entity, but to provide information to help existing and potential investors, lenders, and other creditors to estimate the value of the reporting entity. According to Indonesian Financial Accounting Standard (IFAS[2]) 1, company can also disclose an environment statement and value added statement separately with financial statement; especially for companies which environment factor play as an important role and also for companies which consider the stakeholders as important users of the report.

Disclosure

Disclosure means presenting useful information to those who need it. According by Evan (2003) in Suwardjono (2008), disclosure is the information supply in the financial statement, the notes to the statement, and the supplementary associated with the disclosure statements; whether its public or private statements made by management. The disclosure itself mainly aimed for investors and creditors.

Disclosure is a company's way to present all relevant information to users in order to make them able to estimate the value of the company. The relevant information is not limited on financial-related information, but also non-financial information such as inventory turnover, on time delivery, elapse time between a customer order and productivity delivery, customer preference rankings compare to competitor, response time to a service sell, time to develop new products, employee satisfaction, number of customer complaints (Warren and Reeve, 1997). Some of those items are also written in KEP-431/BL/2013 by BAPEPAM-LK on CSR disclosure section.

There are two bodies in charge of the disclosure standard. The term dual governance structure is commonly used to refer to the existence of the two bodies. BAPEPAM-LK's authority usually limited to the routine reporting such as annual report; while standard constituent body such as FASB is authorized to determine the disclosure format in general financial disclosure. FASB also authorized to determine of the amount of information should be presented in financial report.

[2] IFAS in Indonesia term is PSAK which stands for *Pernyataan Standar Akuntansi*

The three levels of disclosure proposed by Hendriksen and Brenda (1992) are adequate disclosure, fair disclosure, and full disclosure. Those levels are based on how much information disclosed. Some people argued that too much information is harmful. One of the reasons is because it presents unimportant details that could hide the significant information. Too much information also makes the financial reports difficult to interpret. Users may not be able to focus on the priority information they should pay attention. It also may confuse the users with much information that may be irrelevant.

Corporate Social Responsibility

There are two aspects of corporate social responsibility: making a profit and providing social services. Those aspects seems in line with the definition stated by Lantos (2011) that said corporate social responsibility as a social contract between corporations and society, based on long-term social demands and expectations. Some other definitions also make a similar point. Despite the fact that there are so many definitions about CSR, the underlying cause is that CSR involving not only the shareholder, but also the stakeholder. The stakeholder takes their own part on CSR based on their own interest.

Corporate Social Responsibility Disclosure

Ernst and Young (2009) defines non-financial or sustainability reporting as the practice of measuring, disclosing and being accountable to internal and external stakeholders for organizational performance towards the goal of sustainable development. This reporting activity perceived to benefits the organizations in terms of stakeholder engagement and reputation. The non-financial information regulation which may vary in every country makes it harder to compare one disclosure to another. A guideline issued by Global Reporting Initiative (GRI) is the most renowned guidelines used by companies despite the fact that there are so many guidelines available.

Indonesian government regulations also can be used by companies as guideline. Act No. 40 of 2007 give a regulation about including corporate social responsibility- as an example of non-financial information- report in the annual report. Other regulation such as *Keputusan Ketua Badan Pengawas Pasar Modal* *dan Lembaga Keuangan* No. KEP-431/BL/2012 specifically set corporate social responsibility as one of the disclosure items.

Earnings Forecast

Earnings forecast are based on analysts' expectations of company growth and profitability. Hope (2002) documented that financial disclosure quality is positively related to analyst forecast accuracy. Analysts' forecasts mostly used as a proxy for the market's expectation for earnings and practitioners require accurate earnings forecasts in many stock valuation models. Hope (2002) in his research focuses on professional analysts as they are one of the most important users of financial reports. As a result of the uncertainty of earnings forecast, the analysts' forecast error is comprised of an error due to imprecise public information and an error due to imprecise private information.

Hypothesis Development

The relationship between financial information disclosures to earnings forecast is undoubtedly positive. There are many researches on that area since the financial indicators make it easier for analysts to forecast earnings. Since financial information disclosures already help the analysts enough to forecast earnings, the reasons and benefits of disclosing non-financial information is questioned. The non-financial disclosure is merely only for obeying regulations and satisfying stakeholders.

This research wants to specify the non-financial disclosure to the extent of CSR disclosure since Indonesian publicly listed company mandatorily should disclosed its CSR activities. This research will test the relationship between corporate social responsibility and earnings forecast accuracy. The result may imply negative, neutral, or positive relationship. Hence, there is no research resulted in negative relationship between corporate social responsibility disclosure and earnings forecast accuracy yet. However, this research anticipated the negative relationship since Dhaliwal et al. (2012) specifically used stand-alone CSR reports while this research doesn't. Indonesian company more likely issue their CSR disclosure in annual report or sustainability report. Therefore, the hypothesis is as follows:

Ha: Corporate social responsibility disclosure affects earnings forecast accuracy

III. RESEARCH METHODOLOGY

The population of this research is companies listed in Indonesia Stock Exchange. Despite the fact that CSR implementation only mandatory for companies which its business activities and/or has a relation with natural resources according to Indonesian Corporate Act No. 40 of 2007, many other companies with no relation with natural resources implement CSR. From that background, the research does not focus on certain industry but all.

The four criteria should be met are: (1) Companies listed in Indonesia Stock Exchange (IDX) during the period of 2009-2012 respectively; (2) Companies with publicly available earnings estimates for year 2011 and 2012; (3) Companies published CSR disclosure in a form of annual report (sustainability report) and/or stand-alone CSR report on 2010-2011 respectively; (4) Companies providing financial statements on 2009-2012 respectively; (5) Company with publicly available historical stock price on 2011-2011 respectively.

From the total of 327 companies listed in IDX during 2009-2012 respectively, with those criteria, this research will only be using 48 companies each year. The limitation of forecast horizon to a maximum of two years is because most independent parties only provide history of limited period of time.

This research will use 3 variables that consist of 1 dependent variable which is earnings forecast accuracy, 1 independent variable which is CSR disclosure and 1 control variable which is financial opaqueness.

Earnings Forecast Accuracy

In order to get an accuracy measure of a forecast, the researcher decides to use FERROR formula developed by Dhaliwal et al (2012). FERROR represents forecast error as an inverse measure of forecast accuracy. Forecast error (*FERROR*) is defined as average of the absolute errors of all forecasts made in the year for target earnings:

$$FERROR_{i.t} = \frac{1}{N} \sum_{j=1}^{N} |FC_{i,t,j}^{Y} - EPS_{i,t}^{Y}| \,/\, P_{i,t}$$

where subscripts *i*, *t*, and *j* denote firm *i*, year *t*, forecast *j*. FC is analyst earnings forecast, EPS is actual earnings per share, P is stock price at the beginning of the fiscal year, and Y is the indicator to denote the target earnings and the forecasts for the current year (0) or one year ahead (1).

CSR Disclosure

There are some measurements available to be used to measure the CSR disclosure (CSRD). The data measurement used in this research is referring the regulation issued by BAPEPAM through *Keputusan Ketua Badan Pengawas Pasar Modal dan Lembaga Keuangan* No. KEP-431/BL/2012 about The Submission of Annual Report by Listed Companies point 2.h. BAPEPAM standard on CSR disclosure required companies to disclose its CSR activities that cover policies, types of program, and cost incurred on the environmental aspect; employment practices, health and work safety aspect; social and community development aspect; and product responsibility aspect.

Score 1 will be given to each item that disclosed by the company and score 0 is otherwise. The scores from each item later on will be summed up to get a total score for each company.

$$CSRD(Y)_j = \frac{X_{ij}}{n_j}$$

where Xij is the dummy variable when the value 1 is given to the item disclosed and otherwise and nj is the total items should be disclosed according to BAPEPAM standard; which is 12.

Financial Opaqueness

Study done by Hope (2003) finds that firm-level annual report disclosures are positively associated with forecast accuracy. This research posits that CSR-related information is, to a large extent, distinct from financial information because CSR disclosure is mainly directed toward stakeholders (Robert, 1992). For firm with higher level of financial opacity, analyst can gain more useful information from nonfinancial disclosures in assessing the future financial performance of these firms. The computation of financial opaqueness measure *CFIN* as the absolute value of a firm's scaled accruals, averaged, over the prior two years. Scaled accruals (*ACCRUAL*) are calculated using information about current assets (*CA*), current liabilities (*CL*), cash (*CASH*), current portion of long-term debt (*STD*), depreciation and amortization expense (*DEP*), income taxes payable (*TP*), and total assets (*TA*):

$$ACCRUAL_{i,t} = (\Delta CA_{i,t} - \Delta CL_{i,t} - \Delta CASH_{i,t} - \Delta STD_{i,t} -- \Delta DEP_{i,t}) / \Delta TP_{i,t}$$

(Dhaliwal et al, 2010)

In order to reduce the measurement error, the convert of the absolute value of ACCRUAL into CFIN as an indicator variables that takes a value of 1 if a firm's two-year (prior two years) average absolute accrual is greater than the median of the same industry in Indonesia of the period, and 0 otherwise, is needed.

Hypothesis Testing

Aside from the descriptive testing, this research will use four classical test assumption tests. There are normality test with Skewness Ratio, multicollinearity test, Gesjer heteroscedasticity test, and autocorrelation test. While the regression model used is:

$$FERROR = \alpha + \beta\, CSRD + \beta\, CFIN + e$$

where FERROR represents forecast error, CSRD represents CSR disclosure level, CFIN represents firm-level financial transparency, and e represents standard error. The criteria of the hypothesis are: (1) Hypothesis is accepted if the significance level is less than 0,05 (sig. t < α) and β CSRD is negative; and (2) Hypothesis is unaccepted if the significance level is greater than 0,05 (sig. t > α) and β CSRD is not negative

IV. DATA ANALYSIS AND DISCUSSION

Table 4.1

The Effect of Corporate Social Responsibility Disclosure to Earnings Forecast Accuracy with Financial Opaqueness as a Control Variable

Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.430[a]	.185	.167	.02001

ANOVA[b]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	.008	2	.004	10.313	.000[a]
	Residual	.036	91	.000		
	Total	.045	93			

Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	.027	.009		3.177	.002
	CSRD	-.035	.011	-.312	-3.086	.003
	CFIN	.009	.004	.205	2.027	.046

Source: processed data, 2014

Based on the hypothesis testing, researcher is able to derive a multiple linear regression model as follows:

$$FERROR = 0.027 - \ 0.035CSRD + 0.009\ CFIN$$

The significant value of independent variable which is CSR disclosure from the multiple linear regression result is 0.002. If the significant value is less than 0.005, it means that independent variable is significantly affects the dependent variable. Since 0.002 is smaller than 0.005, the researcher infers that CSR disclosure has a significant effect to earnings forecast accuracy (Ha accepted). The beta (β) sign shows the influent of independent variable to dependent variable, whether it is positive or negative.

The negative sign indicates the influence brought by the independent variable to the dependent variable. It means that CSR disclosure negatively influence earnings forecast error. This condition shows that for company which issued more CSR-related information in their CSR disclosure will make analyst earnings forecast error tends to get lower. This result is similar with Dhaliwal et al. (2012) which stated that the issuance of CSR stand-alone reports is associated with lower analysts forecast error. With these results, it proved that the amount of information disclosed in CSR disclosure will affect the earnings forecast accuracy. The relationship of the two things emerge since analysts use as many information as they can get to make a forecast. With sufficient amount of information disclosed, analysts can make a better forecast.

The results of Adjusted R Square value in regression analysis with and without control variable are different. With no control variable the Adjusted R Square is 0.139, while with control variable the Adjusted R Square shows a value of 0.167. This means that with no control variable the CSR disclosure alone only able to explain 13.9% change in earnings forecast accuracy and the other 86.1% are explained by other factors. By having financial opaqueness as control variable helps the CSR disclosure variable to explain a 2.8% more into 16.7% and 83.3% are explained by other factors. It shows that with control variable, the dependent variable can be more explained by it.

V. CONCLUSION

Based on the hypothesis test, the result of the study shows that hypothesis that stated that corporate social responsibility disclosure affect earnings forecast accuracy. The result is supported by empirical evidence which has a significant value from regression model to test CSRD variable where 0.003 < 0.005 which resulted in an accepted hypothesis. The CSRD regression coefficient of negative 0.035 shows the affect value of it to earnings forecast accuracy. Financial opaqueness as control variable is able to control the relation of the model by comparing the regression model with no variable control with the regression model with variable control.

The limitation of this research may incur in subjectivity manner on the measurement of corporate social responsibility disclosure that can cause the result vary. The few indicator items used to measure the CSR disclosure also may become a limitation. Another limitation is since the availability of the data from the source used is limited. The result in such number of companies and horizon may not represent all of the companies.

Suggestion that can be given for further research is: to use the most update and complete CSR disclosure measurement such as the one used by GRI. Another suggestion is to use a bigger amount of companies and larger period of time by looking for another source of data

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